

Tax Reform Study Committee

January 12, 2003
State Capital Building, Rm. 317
Helena, Montana

MINUTES

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed. Committee tapes are on file at the Department of Revenue. Exhibits for this meeting are available upon request.

COMMITTEE MEMBERS PRESENT

Sen. Keith Bales, Chair
Jerry Driscoll
Ken Morrison
Myles Watts
Mary Whittinghill
Rep. Eileen Carney
Rep. Jill Cohenour
Rep. Bob Lake
Rep. Jim Peterson
Sen. Jon Ellingson
Sen. Gary Perry
Sen. Dan Harrington

COMMITTEE MEMBERS EXCUSED

STAFF PRESENT

Larry Finch, Department of Revenue
Dan Dodds, Office of Budget and Policy Planning
Jackie Williams, Department of Revenue
Prudence Gildroy, Secretary

AGENDA & VISITORS

Agenda (ATTACHMENT #1)
Visitor's list (ATTACHMENT #2)

COMMITTEE ACTION

CALL TO ORDER AND ROLL CALL

The meeting was called to order by **Presiding Officer - Senator Keith Bales** at 1:15 p.m. Secretary noted the roll. The minutes of the previous meeting were approved.

Larry Finch, Department of Revenue, and Sen. Bales discussed the agenda. There would be time to present proposals such as that of **Rep. Jim Peterson**. **Sen. Jon Ellingson** assumed **Rep. Peterson** would be talking about a sales tax proposal and there would be an opportunity to talk about a “big box” tax, etc. **Sen. Bales** said they would welcome anything anyone might have. Attention was called to a letter to the committee from **Ken Nordtvedt**, a former legislator and Department of Revenue Director, which provided recommendations to the committee. **Sen. Bales** indicated all the legislators also got a copy of a letter to which the governor replied and he would get copies of the letter and response for the whole committee.

Jeff Martin, Legislative Services Division, presented a report on tax structures of selected states and (some) reform. He defined “fiscal illusion” as the tendency for the public to underestimate the cost of government for a variety of reasons. He noted snow removal, garbage collection, fire and police protection were all paid for by property tax. Sources for his report included Steven Gold, “State Tax Reform in the Early 1990s”, *State Tax Notes*, Vol. 6, No. 17, pp. 1146-1164 and “The Way We Tax”, *Governing*, Vol. 16, No. 5, February 2003, pp. 38-97.

Alabama worked on a tax reform proposal recently. They had a special legislative session and submitted a 600 page legislative package to the electorate called a “tax and accountability referendum”. The package was defeated by a 2-1 margin. Alabama relies on a sales tax and income taxes. They have four separate rates by category. The general rate is about 4%. They allow local option taxes and the rate at the local level can vary with the average about 8%. Regarding property taxes, they have one of the lowest per capita liabilities in the nation. Utilities are taxed at 30% of value. There is a tendency by state legislatures to tax utilities at a higher rate than other kinds of property and it ends up being a hidden tax on consumers. Business property was taxed at 20%, residences at 10% and automobiles at 15%. Agricultural land was taxed at a lower rate. Rates are in the Constitution. The income tax is also capped in the constitution and is not tied to the federal definition of income. Most revenue is dedicated to education, which results in expenditures for public services being given short shrift. In the 1990s, they passed tax incentives to attract automobile manufacturers to the state. They have no tax expenditure report. He didn’t know how far the committee would get into the tax expenditure evaluation, but it seemed to him the attitude of looking at tax expenditures may have changed.

During the 1991 recession, Arizona raised taxes by restructuring the tax rates, broadening the base to be more in line with the federal system and eliminating the federal income tax deduction. These tax increases led to a voter initiative to require a 2/3 majority to raise taxes. Through the 1990s there were \$1 billion in tax cuts. These included lowering personal income taxes with reduced marginal tax rates, lowering the threshold for medical deductions, a \$50,000 personal property tax exemption and setting high rates on business equipment. One of the biggest items was a tax credit for alternative fuel vehicles which was estimated to cost about \$3 million but the real cost was \$200 million. He recalled there was a similar bill introduced in the 2001 session, which allowed the

same kind of deduction in Montana. It made it out of the Senate tax committee but not the House tax committee. Because of the income tax reductions, they are more dependent on the sales tax and there are a lot of local option taxes. There is a lot of variability in rates as well as the items subject to tax. The cigarette tax was increased by ballot initiative in November. Recommendations are due from the Tax Reform for Arizona Citizens Committee. Poor technology hampers Department of Revenue in compliance and analysis. They are reorganizing to have a management system based on functional efforts rather than tax type and are working on an integrated tax information system. **Mr. Finch** commented the fuel tax credit was one of the biggest snafus ever done by a legislature. One of the things that got qualified as an alternative fuel vehicle was golf carts. Because of the way the refundable credit worked, the state of Arizona ended up purchasing thousands of golf carts.

Arkansas has a regressive sales tax where food and over-the-counter medicine are subject to tax. He didn't know if this included prescription drugs. Voters had an opportunity in November 2002 to exempt these items from the sales tax and chose not to do so. The schoolfunding lawsuit may have made that a wise decision. (*Tape 1, Side B*) In 1997, they cut income tax on poorer taxpayers. In 1999, they exempted the first 30% of capital gains income from taxation, gave a \$300 individual property tax credit and raised the sales tax to pay for the credit. Arkansas requires a $\frac{3}{4}$ majority vote to raise taxes. This applies only to taxes in effect in 1934 and a sales tax was not imposed at that time. In the early 1990s they added selected services to the sales tax. Income tax is not tied to the federal definition of adjusted gross income. Their technology and administration of taxes is out of date.

California has one of the more progressive and volatile income tax structures. Almost 50% of state tax collections in 2001 came from individual income taxes. He was not sure of the fund structure so didn't know what percentage of income taxes are in the general fund. The top tax rate is 9.3% and capital gains are taxed as ordinary income. The stock market collapse had a significant impact on state income tax collections. They increased top marginal rates in the early 1990s. Proposition 98 set minimum expenditures for primary and secondary education and community colleges to a 5% a year increase. An after-school program by Governor Schwarzenegger may also have an impact on their general fund budget. Tax subsidies are used to garner votes for the budget. Proposition 13 and limits on local option sales taxes means local governments depend on largesse from Sacramento. A $\frac{2}{3}$ majority is required to pass budget or tax increases. The Franchise Tax Board administers corporate and individual income taxes and the Board of Equalization, which includes legislative members, handles sales tax, local property tax oversight and the appeals process. California purported to have a good corporate tax structure. **Sen. Harrington** commented in California they are allowed to borrow money to pay off their deficit. **Mr. Martin** thought their bond rating had probably declined.

Colorado has a taxpayer's bill of rights passed by citizen initiative in 1992 which restricts increases in state and local taxes without voter approval. State revenue growth is limited to the sum of inflation and population increase and local revenue growth is limited to the sum of inflation and increases in new construction. Excess revenue collections are

refunded to taxpayers. Voter approval is required to allow the state to keep excess. Local governments are more successful at this than the state. In 2002, \$927 million was refunded despite large declines in the individual income tax and corporation tax. There is a single subject requirement in their constitution. A strong economy led to sales and income tax cuts by the legislature in the last several years. A tax study commission was created but was not funded. Local governments are heavily reliant on local option sales taxes.

Idaho had a strong economy in the early 1990s and dodged the recession. They cut individual and corporation taxes in 2001, which decreased revenue by 14.5%. Their problems are cyclical rather than structural. A Blue Ribbon Tax Commission was established in 2002 and was supposed to look at sales tax exemptions. The *Spokesman Review* chastised the committee for shirking its responsibilities, especially in light of a temporary sales tax increase due to expire in mid-2005.

Illinois has the highest average property taxes in the nation on \$150,00 residences because of school funding and the state is the third lowest in state support for schools. Their constitution requires a flat income tax rate, currently set at 3%, and the corporate income tax may not exceed 8/5 of the individual income tax rate. There is a single-sales formula for corporate income tax and there is an erosion of the base. They suffered greatly from the recession. **Sen. Perry** asked about the single rate and **Mr. Martin** indicated he didn't know what the rate was. **Sen. Perry** said he might be interested to see the different tax rates. **Mr. Martin** said one reason for high property taxes was a good portion of the property tax goes to school funding and there is no significant state support for schools. **Ken Morrison** commented they exempt personal property. **Rep. Bob Lake** asked about the retirees' income exemptions and the lawsuit *Davis v. Michigan*. **Mr. Martin** replied that back in the early 1990s a federal retiree in Michigan sued the Department of Revenue claiming it couldn't tax his federal retirement income at a higher level than state employees. Davis prevailed and he didn't know if Illinois had always exempted retirement income or if it was the result of this decision. **Rep. Lake** asked if it was just state and federal income and **Mr. Martin** advised it says all retirement income—federal, state and private. Mississippi exempts all retirement income as a specific strategy to attract retirees to the state. **Sen. Harrington** recalled state employees were already exempt and federal retirees filed the suit. **Mr. Martin** said it was a significant political controversy when it came up. The alternatives were to exempt at least federal retirement income from taxation matched with state and leave private retirees at the \$3600 exemption or tax everybody the same. Exempting federal retirees would cost a lot more than taxing everybody the same.

Massachusetts tax rates rank in the middle of all states. Individual income tax increased from 5.76% to 5.9% in 1990 and sales tax was expanded to most services. Governor William Weld repealed the new tax on services the day after they went into effect. Taxes were cut in the 1990s and a voter initiative in 2000 further reduced income taxes to 5% over 3 years. Because of declining revenue related to the stock market, the legislature froze the income tax rate at 5.3%, eliminated the charitable donations deduction, and reduced personal exemptions. They revised regulations to tax capital gains as ordinary

income and increased the cigarette tax. The state provides revenue to local governments because of a cap on local property taxes (Proposition 2) approved by voters in the 1980s.

Michigan lowered the property tax and raised sales taxes in 1994. The state pays 78% of school funding whereas they paid 29% before the change. Local tax changes there require legislative approval. Other changes included repeal of the intangibles tax on dividends and interest, increased personal exemptions for income taxes, higher deductions for children, tax breaks for older taxpayers, a planned 5-year reduction in income tax rates and a 20-year phase-out of the single business tax—similar to a value added tax. The single business tax, in place since the 1960s, replaced a variety of other business taxes. Another provision was to halt the phase-out temporarily if the rainy day fund got below \$250 million. In 2002 the phase out was accelerated to 2010 with a presumptive replacement by something else.

Nevada is dependent on gambling revenue and it has been declining on a per capita and per visitor basis since the mid-1990s. They have a narrow-based sales tax which has been affected by the recession and internet sales and they have no income tax. A property tax cap was imposed in 1981. New taxes or increased taxes require a 2/3 vote in each house. Voter approval is required for changes previously approved by the electorate. Nevada established a Task Force on Tax Policy in 2001. The last tax study in the late 1980s was largely ignored. In a special session in 2003 they imposed a modified business tax of 0.7% on gross wages for general employers and 2% on financial institutions; a live entertainment tax; (*Tape 2, Side A*) expanded the real property transfer tax; revised the cigarette, liquor and alcoholic beverage taxes, insurance premiums and a tire surcharge; and instituted a bank excise tax of \$1750 for each branch in excess of one branch.

The sales tax in New Mexico is a gross receipts tax on a broad range of goods and services including food and prescription drugs. In the early 1990s they had a tax rebate for purchases made for those items. Everyone was eligible based on income level and number of dependents. They eliminated the credit in the early 1990s to increase the federal match for Medicaid funds. They still provided a low income tax credit. Sales to the federal and local governments can be taxed. The gross receipts tax is used primarily to fund education. Recently they had a phased in reduction of the top marginal income tax rate from 9.2% to 4.9% and expanded the capital gains deduction. They also created a Blue Ribbon Tax Reform Commission, which made recommendations to increase taxes and fees by \$130 million. Those recommendations were rejected by the legislature during a special session in October of 2003. The recommendations included not to reduce or eliminate the gross receipts tax on foods, not to increase the excise tax on liquor, to tax non-profits (e.g., Los Alamos National Laboratory), and recommended phasing out the capital gains deduction for high income taxpayers that had been enacted in the 2003 session. Each year there is a bigger deduction based on the percentage increase of the amount of capital gains.

Oregon is heavily reliant on the income tax for general fund spending. A ballot initiative shifted most public school funding from local property taxes to the state, about 66%. The

measure froze property values at 1995 levels. Local governments may not increase tax rates without voter approval. There is a refund mechanism if state revenue collections are in excess of 2% of the estimate. Corporation income tax collections are credited if income tax collections are in excess of 2% of the estimate. September 11th and the recession severely affected tax collections. They enacted HB 2152 that imposed a graduated personal income tax surcharge, increased the corporation minimum income tax from \$10 to \$250, extended the 10 cent a pack cigarette tax, and reduced the discount for property taxes paid in November. A voter initiative placed legislation on the ballot for a special election on February 3, 2004.

Utah's constitution dedicates income tax to education and 53% of local property taxes go to education. There have been no tax increases over the last ten years. The sales tax is a declining source of revenue. There is a limited taxation of services. Eliminating the exemption for car wash establishments met with strong opposition.

Washington has no income tax and their primary sources of revenue are the sales tax and business occupation tax. The business occupation tax is basically a gross receipts tax on sales and the rate is dependent on a classification scheme by industrial sector. The rates are below 1% to try to mitigate pyramiding. The tax is paid regardless of the profitability of the business. Washington was one of the first states to offer electronic filing on the Internet. The state will complete tax returns from business spreadsheets. A system is available to calculate sales tax by taxing district. Similar systems might be applicable to intra-state sales tax calculations.

Wyoming has a balanced system—sales tax, severance taxes, and interest from the mineral trust fund. The trust fund contributes a little over 13% of total general fund revenue. In 1999, because of falling energy prices, the state had a large revenue shortfall and was seriously considering an income tax. A rise in energy prices helped with state revenue collections and the state ended up with a large surplus. A school finance decision mandated more equitable school funding. There was a disparity in mineral rich counties. Minerals are taxed at 100% of value while residences and business property are taxed at 9.5% of value. The sales tax is at 4% and includes food and selected services except for professional services. They attempted to expand the sales tax to more services but there were objections.

Questions from the Committee

Mary Whittinghill noted some states have attempted to expand the sales tax to other services and she wondered if there were any studies on that. **Mr. Martin** replied Florida is an interesting case. They expanded the sales tax to virtually every service in the late 1980s. Collections exceeded projections. One of the things that led to the collapse of the tax on services was the tax on advertising. Advertising that came from out of state started the ball rolling on repealing the measure. The early 1990s recession and the current recession bracket the tax changes between the two recessions. A lot of tax decreases in that period were understandable given the economic situation. Changes to the tax rates and cuts made over the period were applied mostly to progressive taxes like

the income tax or regressive taxes like sales taxes. There are similarities between the period right now and the period that started the decade of the 1990s.

Sen. Bales asked **Mr. Martin** if he had a sense of a system in any one of the states that seemed to be favorable to residents of the state or if most people were unhappy with taxation no matter what. **Mr. Martin** indicated outside observers say New Mexico has an ideal system. South Dakota does not have an income tax system and relies heavily on the sales tax.

Ms. Whittinghill commented New Mexico's governor advertised income tax reform. **Mr. Martin** recalled they tried to put in an integrated tax system, which didn't work. It was replaced in 2002. **Ms. Whittinghill** wanted to know if the advertising was successful. **Mr. Martin** thought any economic effects would be year away from being measured.

Sen. Ellingson said that raised an issue at the heart of what this committee is trying to get to—not only a tax system that everybody likes but also a tax system that stimulates economic development in the state. He asked how effective states can be in stimulating economic development through the tax structure. **Mr. Martin** said a systematic analysis would be needed. **Sen. Ellingson** asked if there are such studies and said he would be interested in seeing those. There is wild optimism about what might happen but he had yet to see a study that clearly delineates what can be done and what impact can be expected. States are dependent not only on what is going on in the economy in the United States but also on the world market. **Mr. Martin** said he could track down studies but those would need to be evaluated. **Sen. Ellingson** reiterated he would like to see those studies and **Mr. Martin** said he would see what he could do.

Sen. Bales commented there are the efforts of reducing or changing taxes to attract businesses or industry and taxes that are enacted whether intentionally or unintentionally to drive businesses out. He didn't know if studies address that or not. (*Tape 2, Side B*) **Myles Watts** encouraged finding summaries rather than exhaustive reviews. **Sen. Ellingson** said he would be satisfied with that but felt it was at the core of the committee's considerations. **Mr. Finch** agreed with **Mr. Watts** there is a tremendous amount of work on these issues that establish a relationship between taxation, particular types of tax structures and the influence those things have on economics and business development. It is a huge job to examine it all. **Mr. Martin** noted for every study there is a point and counterpoint. There may be some studies where there are agreements. **Mr. Finch** indicated some studies are better than other studies. Some are more scientific and some are based on conjecture. **Rep. Lake** stated there is a risk in taking a study from another state and situation regarding economic development. Some parts of such a study are probably valid for Montana. **Mr. Watts** advised there are 100 mainline economists that would give about the same overall general indication of how important taxes are to economic development. **Rep. Peterson** wondered if there is any trend or movement toward or away from the three-legged stool approach and if other states were eliminating one tax in favor of another or moving toward a more balanced system. **Mr. Martin** said he couldn't answer definitively. He noticed changes in tax rates during the 1990s tended

to reduce progressive or regressive taxes. His sense was there was a movement more toward the income tax side than the sales tax side. He noticed even with tax rate reductions in the period, revenues had gone up.

- **Break** – 3:00 p.m.

- **Reconvene** – 3:15 p.m.

Dan Dodds, Office of Budget Policy and Planning, presented a report of state tax revenue and distribution for 2003 and 2004. Individual income tax is the largest state revenue source and collections in 2003 were about \$536 million with 100% distribution to the general fund. The second largest source was motor fuels taxes, which brought in about \$193 million. Just over 95% was distributed to the highway special revenue fund, just under 5% to other Department of Transportation funds and 0.1% to the noxious weed management trust. Taxes collected on off-highway use are available for other uses. In answer to a question by **Sen. Bales**, **Mr. Dodds** indicated distribution is set in law and is not tied to actual collections. At least 5% of motor fuel taxes are from off-road uses. There is no earmarking of aviation fuel to certain uses. Some of the smaller revenue sources are going into the general fund or to one use. Vehicle taxes are all going to the general fund. Property taxes are going primarily to the general fund with smaller allocations to the University system. The Accommodations Tax has the most complicated distribution. For 2003, due to action in the special session, 14.24% goes to the general fund. Oil and gas taxes changed from 2003 to 2004. In 2003 and prior years, each type of well and production was split between state share and local share. The local share was allocated based on mill levies. In the last session that was changed so everything is straight percentage. Each county gets a percentage of revenue from that county and it goes to county uses and the state share goes to various funds in fixed percentages.

Ms. Whittinghill asked if vehicle taxes are fees. **Mr. Dodds** indicated taxes and fees were split. Part of the license fee is considered property tax and then there are fees that used to be property tax on a vehicle. **Mr. Finch** advised taxes would include those things that were a flat fee.

Mr. Dodds continued that most of the taxes were distributed in a percentage allocation system, the oil and gas tax as an example. Regarding property taxes, mill levies are allocated differently with 95 mills going to the general fund, 6 mills going to the University System and an assessment per acre which is not the same throughout the state that goes for forest fire protection. Some of them are allocated mostly in fixed dollar amounts. The resource indemnity tax is fixed dollar allocations. Revenue is projected to be over a million dollars. \$431,000 goes to repaying bonds for the Libby clean up. \$366,000 goes to the Bureau of Mines groundwater assessment program and the remainder goes to grants and displaced workers scholarships and orphan shares.

Sen. Bales asked why oil and gas production is no longer broken out and 90% goes to the general fund. He thought some of that still went to the counties and to the schools. **Mr. Dodds** indicated the county share comes out first for each county but that percentage is

different for each county so he didn't list them all. The money that formerly went out to the counties and then came back to the state with the 95 mills now stays with the state. The amount that stays in the counties is the same. That is about 50% statewide, but that other 9% used to go out to the counties and then come back.

Sen. Perry asked about the estate tax. **Mr. Dodds** said the estate tax was based on the credit that the federal estate tax allowed for the state tax. The inheritance tax was repealed just after the end of 2000. The estate tax is going away because the federal tax is being phased out. The tax is expected to come in at lower levels for a few years. **Mr. Finch** said it will slowly trend downward.

(Tape 3, Side A)

Mr. Dodds explained a table of fees collected by state agencies. The work was done in conjunction with **Mary Whittinghill** and **Terry Johnson**. The table included a broad conception of fees—anything that was not a tax, interest earnings or employee contributions for health insurance or pensions. They tried to exclude intragovernmental fees that agencies pay to the Department of Administration or other agencies for the computer network or their share of the state accounting system, rent, telephone, etc. The largest category was fees paid to the University system, which included both fees paid by students and funding received from other sources for services performed by the universities. This would include payments to the University System for grants and contracts. The second largest category was worker's comp premiums.

Mr. Driscoll asked about unemployment insurance premiums. **Mr. Finch** suggested an explanation of the various taxes and fees. **Mr. Dodds** explained the individual income taxes were self-explanatory. Vehicle taxes were part of what is paid for a vehicle license. **Mr. Finch** added that the increase from FY 2003 to FY 2004 was a result of legislation that provided for permanent registration of certain types of recreational vehicles, snowmobiles, etc. **Rep. Lake** asked if this included the GVW and **Mr. Finch** said no, that is a fee and not a tax. **Ms. Whittinghill** said it isn't necessarily a property tax anymore. It went from value and now is based on the age of the vehicle. The distinction being it is not deductible on the federal return. The \$4 optional tax was included in 2004. **Mr. Finch** indicated a number of fees were combined into the registration fee, which goes into the general fund. **Mr. Dodds** said the Corporate Income Tax is on the income of corporations. Insurance taxes are taxes on insurance premiums. There is a tax on all insurance premiums and an additional tax on fire and casualty. The Retail Telecommunications Excise Tax appears on phone bills and is a tax on charges paid for telephone service. The sales tax on accommodations is the new 3% sales tax from SB 407 and goes to the general fund. The estate tax will go away. The Electric Energy Production License Tax and Wholesale Energy Transactions Tax are taxes on electricity production and transmission. The Contractor's Gross Receipts Tax is a tax on the gross receipts of contractors, which is then a credit against their income tax. **Mr. Finch** indicated it is a 1% tax that applies only to contracts on public works projects. **Rep. Peterson** asked if this only applies to Montana contractors doing public works projects and **Mr. Finch** advised any contractors—mostly for highways. **Mr. Driscoll** commented this was put in because out of state contractors weren't paying personal property taxes

and Montana contractors were. **Mr. Finch** advised this is the net that comes in from the 1% after the refunds for property tax receipts. **Mr. Dodds** continued the rental car tax is the new 4% sales tax resulting from SB 407. The Rail Car Tax is a property tax on rail cars. **Ms. Whittinghill** indicated rail cars are mostly not owned by the railroads and the tax is based on the average mills. **Mr. Dodds** went on to say the Cement and Gypsum tax is a tax on the production of cement and gypsum. The Attorney License Tax is called a tax but looks exactly like other business and professional licenses that are called licenses. The Custom Combine Tax is like the Rail Car Tax.

Rep. Lake asked what it costs to collect that tax and wondered whether or not the tax is worth it. **Mr. Finch** had no idea what it costs. **Rep. Peterson** asked if it is collected when they come into the state and go through customs and have to fill out a form. He wondered how the department knows they are here. **Mr. Dodds** said they pay GVW fees, etc. **Mr. Finch** indicated it is a registration issue as much as a tax issue. **Mr. Dodds** continued Motor Fuel Taxes are a tax on gasoline, diesel, aviation fuel, and special fuel such as propane. Diesel goes 100% to the DOT for the highways special revenue account, and gasoline goes 98% to the DOT for highways and small percentages go to other accounts. Property tax is strictly what is on mills—95 mills collected for schools goes to the general fund and 6 mills for the University System going to the universities. Oil and Gas Production Tax is a percentage tax on oil and gas that is produced and is distributed in fixed percentages to counties, schools and state government. In answer to a question by **Rep. Cohenour**, **Mr. Dodds** indicated it is a volatile tax and collections go up and down. Gambling taxes are what the state collects from video game machines. There is also a tax on bingo and keno that goes to local government. **Rep. Lake** asked if this includes the profit that the lottery returns to the state. **Mr. Dodds** advised that is listed in fees. They use a broad definition of fees. Responding to a question by **Sen. Bales**, he indicated before HB 124 there was a state/local split for video gambling. Now local government gets a fixed portion. The Coal Severance Tax is a percentage tax on the value of coal production—50% flows into the coal tax trust fund and a little over a quarter goes to the general fund; 12% to the Long Range Building Program; 7.75% goes to an account the legislature allocates to a number of uses for local impacts; 1.27% goes to the Parks Acquisition Trust; 0.95% to the Renewable Resource Bond Debt Service and 0.63% to the Cultural and Aesthetic Trust. Regarding Alcoholic Beverage Taxes, certain percentages go to the general fund and part to the Department of Public Health and Human Services (DPHHS) for alcoholism related services. Tobacco taxes go to the general fund and for cigarette taxes the greater of 8.3% or \$2 million goes to the Veterans Home, 4.3% to the Long Range Building Program and the remainder to the general fund. The Cigarette Tax is a flat tax per pack and tobacco taxes for chew is a tax per can and for other tobacco products is a percentage. The Accommodations Tax is 4% and SB 407 added to it. Administration costs come out of the tax instead of out of the general fund. The remainder is allocated for tourism promotion at the state and local level and a little to state parks for historical markers, etc. The Metal Mines License Tax is a percentage tax on the value of production from metal mines—58% goes to the general fund and 24% goes to the counties that are impacted by mining and the remainder goes to reclamation and the hard rock mining impact trust. **Mr. Driscoll** asked why the revenue has dropped. **Mr. Dodds**

advised the main reason is in 2003 the tax went from being collected once a year to being collected every six months. In 2003, there was a collection for 18 months. Another reason is that some mines nearing the end of their productive life. **Mr. Driscoll** asked about Butte and **Mr. Dodds** indicated it is not included in the projection. Health Care Facility and Utilization Fees are a set of fees that are charged nursing homes and a couple of the state institutions per bed day. There is a fee they pay for each person in the facility per day. Revenue from state facilities goes primarily to DPHHS and the rest to the general fund; for private facilities it is the other way around. The funds that go to DPHHS are used to pay for the state's Medicaid match. The 911 phone fee shows up on phone bills. It is a fee per access line and a small percentage of it goes to the general fund. Most of it goes to pay for the 911 program. Livestock taxes are per capita fees on livestock and they go entirely to fund the Department of Livestock. Agricultural Commodity Assessments are taxes per unit on a number of different agricultural commodities. The milk assessment goes to pay for the Dairy Inspection Program and the others go to Agriculture Research and Marketing. The Public Service Commission Tax is a tax on utilities that are regulated by the Public Service Commission. The rate is set every year based on what the Department of Revenue projects needs to be paid for the PSC's budget. The Resource Indemnity Tax is a tax imposed on mineral production. The rates vary depending on what the mineral is. There is a fixed dollar amount allocated to various funds. The TDD phone fee is similar to the 911 fee—it is a flat fee on phone bills which funds the telecommunication devices for the deaf. The Consumer Council tax is the equivalent of the PSC tax and goes to pay for the Consumer Council. Half of the Fertilizer Tax revenue is distributed to MSU Extension and half to MSU Agricultural Research. The Airport Tax is from the West Yellowstone airport run by the state and 100% of the revenue goes to the Aeronautics Division.

In response to a question by **Ms. Whittinghill**, **Mr. Dodds** advised the utilities are required to spend a certain amount on conservation and low-income assistance. If they don't use it, it comes to the state for similar programs. **Sen. Bales** asked about the Resource Indemnity Trust Fund. The fund is capped at \$100 million and he wondered if this is separate from the oil and gas tax. **Mr. Dodds** indicated oil and gas doesn't pay it—the Oil and Gas Tax was set up to replace other taxes. A portion goes to the same entity. **Sen. Bales** asked who pays. **Mr. Dodds** advised coal mines and metal mines that are too small to pay the metal mines tax and all other miscellaneous mines.

Rep. Cohenour asked about projections on fees for 2004. **Mr. Dodds** said vehicle fees would increase. **Mr. Driscoll** asked why they think gambling taxes would go up. **Sen. Ellingson** wondered why the corporation license fee would go up \$20 million. **Mr. Dodds** indicated those were initial estimates.

(Tape 3, Side B)

Mr. Driscoll said if dial-up had ever worked, gambling machine owners got credit. He didn't know anybody that actually got the credit.

Sen. Perry asked a question regarding liquor store expenditures. He wanted to know the ratio of liquor store expenditures to revenues from liquor enterprises. **Mr. Dodds** replied

the profits from the liquor enterprise last year were about \$6 million on sales of approximately \$60 million. Expenses for the liquor enterprises were \$54 million. **Rep. Lake** commented that includes the cost of materials and there is no breakdown of operation costs. He wondered if **Sen. Perry's** question was regarding the operation costs of state liquor stores. **Sen. Perry** advised people are paying twice as much for liquor in Montana than in any other states and he wondered about the liquor store expenses. Furthermore, 22-31% of the taxes are being spent by DPHHS on alcoholism. It was a question in his mind as to what the state is doing and if they are doing it right. **Mr. Finch** advised the Liquor Enterprise Division provides an annual report and he offered it to the committee. **Sen. Bales** said the alcoholic beverage tax is \$19 million and he wondered if that does not take into account any profit or loss from operating liquor stores and **Mr. Dodds** said that was correct. When a bottle of liquor is purchased, you are paying what the state pays plus the cost of operating the liquor enterprise, the liquor store markup, plus the tax. **Mr. Driscoll** advised the state warehouse marks it up 40%, there is a 16% tax and a 10% tax to cure drunks. That is why it costs so much in Montana for alcohol compared to other states. The markup is 66%. The state does not do retail any longer; those stores are individually owned. The warehouse ships the liquor to the retailer. **Sen. Perry** asked about the markup at the warehouse. **Mr. Driscoll** said they mark it up 40% and then put taxes on it. The bars get a 8% discount off the suggested retail for having a liquor license. The liquor stores don't get that deal. **Sen. Bales** asked about the amount of profit made by the state liquor warehouse. **Mr. Driscoll** advised it comes out of the 40%. **Mr. Finch** advised the profit would be in alcohol sales. **Mr. Driscoll** indicated the 16% tax is for the general fund. **Rep. Peterson** asked if all the state liquor stores are required to buy from the state warehouse. **Mr. Driscoll** said yes. **Rep. Peterson** said it is a controlled market. **Mr. Driscoll** recalled one store owner could sell 2.5% above what he paid the state and after paying insurance, rent, etc. he was going broke and started raising his prices. **Sen. Bales** advised bringing the report.

Mr. Dodds continued the discussion on fees. Fees for services are fees state agencies charge when doing something for people. The state hospital and other institutions collected \$21 million in charges for providing care. Some of this was paid by the patient and some was paid by the federal government through Medicaid and Medicare. Contributions employees made to buy back years of retirement or to contribute to their medical account was \$18 million. About \$7 million was for various assessment programs, \$3.5 million was for providing various records to the public, \$5 million was federal reimbursement for fire fighting. Parks and Recreation is all of the fees collected by the Department of Fish, Wildlife and Parks such as fishing licenses, campgrounds and state parks, etc. It also includes admissions at the Historical Society. Leases, Rentals and Royalties fees are primarily income from state lands—mineral royalties, grazing and agricultural leases, etc. State sales include publications, revenue from sales of electricity from dams, the prison industry sales, and timber sold on state lands. **Ms. Whittinghill** asked about the total of the fees. **Mr. Morrison** said it was over \$800 million. **Ms. Whittinghill** expressed concern about double counting for amounts coming into the general fund. **Mr. Dodds** indicated those would only show up once on SABHRS. **Sen. Bales** asked how it was determined whether to put them in as fees, etc. **Mr. Dodds** said they didn't include transfers. They looked at where the state was providing services in

return. **Rep. Lake** asked how much goes to the general fund for use. **Mr. Dodds** indicated he could get that number but a lot is collected by agencies and doesn't go to the general fund at all. **Rep. Lake** asked how much is usable in the general fund for state operations. **Mr. Dodds** repeated he could get that figure.

Ms. Whittinghill asked about \$1.3 million in transfers and if those were included. **Mr. Dodds** said they tried to exclude transfers of funds. Some federal money is included in the fees.

Sen. Bales asked for public comment. **Gary Wiens, Montana Electric Co-operatives' Association**, addressed the discussion of the utility property taxes. Electric co-operatives pay three different tax rates in the state of Montana they pay 12% to cities and towns of over 3500 on utility property that was acquired after 1996. They pay 8% to cities and towns over 3500 population where they serve less than 95% of those customers and pay 3% in all other areas. Regarding the burden of property tax paid by customers, there was a study of the issue in 2001. Co-op customers at the residential level pay a slightly higher burden compared to Northwestern customers. The reason for that is the customer density and the miles of power lines compared to Northwestern. The co-ops have about 2.3 customers per mile of power line across the state compared to 12 of Northwestern per mile. Co-ops serve over 40,000 miles of line compared to 16,000 for Northwestern. If property tax rates were ramped up for co-ops it would mean a disparity in the tax burden.

Sen. Bales adjourned the meeting at 4:50 p.m.

Minutes read and approved by: _____
Senator Keith Bales, Presiding Officer Date